Comment Sheet
CVP Cost Allocation Meeting of August 9, 2013

Name: Jerry Toenyes

Organization and Address: Northern California Power Agency, 651 Commerce Drive, Roseville, CA 95678

Phone: (916) 781-4297
Email: **Jerry.Toenyes@ncpa.com**

Comments

NCPA provides the following comments on the material presented at the August 9, 2013 meeting:

1. Final Allocation: NCPA supports Reclamation's decision to make this the final cost allocation for the CVP.

2. Justifiable Expenditure: The purpose of updating the CVP cost allocation is to align project costs with the future operations/benefits of the project. This prospective approach has been used by Reclamation in both the 1970 and 1975 CVP cost allocations and should be the basis for this cost allocation.

We believe the option presented at the August 9th meeting as well as previous ones to potentially use historical benefits distorts the accuracy of the cost allocation process. The top slide on page 5 of the presentation states that the justifiable expenditure represents the maximum amount to be allocated to each project purpose and states that it is calculated as the lesser of the multi-purpose project benefits or the single-purpose project cost for each purpose. This is the basic tenet of the separable cost – remaining benefits allocation methodology. The bottom slide on page 5 states that if future benefits are greater than the single-purpose alternative, the justifiable expenditure is equal to the single purpose costs. This comports with the definition of justifiable expenditure.

The top slide on page 6, however, states that if future benefits are less than the single-purpose cost historic benefits will then be used to increase the total benefits. We believe this proposal is a clear manipulation of the cost allocation process. It is like stating on the bottom slide of page 5 that if the future benefits are greater than the single-purpose cost a different historical cost index will be used to increase the single-purpose cost alternative.

When Reclamation allocates costs for a new project it uses the future benefits or the single purpose alternative, whichever is less, to determine the justifiable expenditure. The separable cost – remaining benefits cost allocation methodology does not allow benefits to be inflated simply because they are less than the single purpose cost. Cost allocations should not be unilaterally adjusted to accomplish some preconceived outcome and should focus on a forward looking (i.e., prospective) analysis.

Reclamation made an early decision in this cost allocation process to eliminate costs from being allocated to navigation, one of the three highest priority authorized project purposes, because navigation benefits will no longer be provided by the CVP. That is a forward looking decision on benefits provided by the project. Yet Reclamation proposes to reverse the forward looking process when analyzing power and water benefits and potentially use historical benefits based on unsupportable criteria. This shows a lack of consistency in the treatment of the various project purposes and an attempt to control the results of the separable costs – remaining benefits process.

Reclamation has already analyzed the flood control project purpose and revealed that flood control benefits will greatly exceed the single-purpose cost. Thus, the single-purpose cost establishes the maximum allocation. Water and power benefits, however, will likely be less than the single purpose cost and adding historical benefits increases the justifiable expenditure for power and water. The probable result of using historical benefits will be to increase the costs allocated to power and water and decrease the allocated costs to flood control. Inclusion of historic power and water benefits appears to be an attempt by Reclamation to modify the cost allocation process to assign more costs to power and water for repayment.

While the proposed use of historical power and water benefits clearly deviates from separable costs - remaining benefits cost allocation methodology, using historical power benefits may require an environmental impact statement to evaluate socioeconomic and environmental justice impacts. First, some of the customers who received historical CVP power no longer exist (for example Mather and McClellan Air Force Bases). Any historical benefits that may accrue because of past CVP power deliveries to those entities would be used to allocate costs to current and future power customers. Current and future power customers would be unfairly burdened by an increase in allocated costs caused by historic benefits received by another entity. This unjust increase would need to be analyzed to determine socioeconomic and environmental justice impacts.

Similarly, Western issued 1984, 2004, and 2014 marketing plans to allocate power to new customers and change the allocation percentages for existing customers. The 2014 marketing plan also contains significant changes in power allocation percentages to all existing customers because of the expiration of a WAPA/customer settlement agreement. Thus, each marketing plan changed the proportion of CVP power received by all customers. Any attempt to use historical power benefits would cause costs to be disproportionally allocated to each customer because the new allocation percentages are different from the historical allocation amounts. Some customers would be allocated future costs for repayment based on historical benefits received by others. Besides being clearly inequitable, the socioeconomic and environmental justice impact caused by using historical data to improperly allocate future costs would need to be analyzed for each customer.

The ability to determine historical power benefits is also problematic. Market data exists for power generation on an hourly basis starting in April 1998 when the California Independent System Operator (CAISO) became operational. Prior to April 1998, power was sold using bilateral contracts between parties based on rates that were agreeable by the parties. The rates contained in those contracts varied greatly and thus any determination of a power value for a particular year prior to 1998 is speculative.

From 1990 to 2000 and from 2008 to date, the cost of CVP power was very close to the market rate. Thus, the net historical power benefit remaining after the cost of CVP power is deducted yields little or no net historic benefit to be used for those years. During the 2000 and 2001 energy crises and the lingering years thereafter, however, the difference between the cost of CVP power and the market rates were substantial. As history has shown the sharp spike in the market price during this era was caused by a faulty CAISO market design and by market manipulation. The State of California has pursued refunds for years from many market participants for that time period and has reached settlement with several of them. In the last few months, more than ten years after the crisis, the State reached settlement with two participants for approximately $1.2 billion for transactions during that era. Some of the entities accused of market manipulation, such as Enron, went bankrupt before refunds could be achieved. Without the "perfect storm" that happened during that era market prices would have been significantly lower. History has shown that market rates were unjust and unreasonable for that period and no one can recreate what the true market price should have been. This is another example of why power and water customers object to using any historical benefits in the cost allocation study as those perceived benefits are inaccurate, speculative, unjust, and unreasonable.

Reclamation knows that future water operations will be significantly different from historical operations because water priorities have changed to meet environmental objectives. The purpose of updating the cost allocation is to align the project costs with the benefits resulting from the changed project operation. Any attempt to control the cost allocation process to allocate more costs to a project purpose than what the future benefits support is clearly inappropriate and will likely yield unsustainable above market pricing.

3. Determination of Future Water and Power Deliveries: We are almost half way through the CVP cost allocation time frame and Reclamation has not yet begun to address how it will evaluate future power and water deliveries in the benefit and single purpose cost analyses. Estimating future power and water accomplishments is contingent on establishing an environmental baseline on a going forward basis. Without such a baseline, future power and water benefits, based on projected water deliveries, cannot be reliably quantified. The continued reduction of power and water deliveries to meet other purposes of water quality, water temperature, fishery requirements, the Coordinated Operating Agreement, the Central Valley Project Improvement Act, the Endangered Species Act, and other criteria must be incorporated into the projections. In addition proposed Delta Flow Criteria, recent decisions by Reclamation to release additional water down the Trinity River above that required in the Record of Decision and generation by-pass releases also need to be considered. Obviously, whatever environmental operating assumptions are ultimately assumed and used will be critical to the cost allocation study. Getting consensus on these critical power and water delivery projections will require good estimating techniques and take more than one meeting to discuss.

4. Alternative Cost Allocation Option: The Central Valley Project Water Association and NCPA sent letters to Reclamation on March 21, 2006 and March 21, 2008 regarding administrative solutions to updating the CVP cost allocation. Those letters are attached. Since we are now 3 years into the process and few decisions have been made, we believe Reclamation should consider using those proposed administrative solutions for this final cost allocation.